DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

OFFICE OF
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INTERNAL REVENUE SERVICE NATIONAL OFFICE FIELD SERVICE ADVICE

MEMORANDUM FOR AREA COUNSEL (HEAVY MANUFACTURING AND TRANSPORTATION: EDISON)

FROM: Assistant to the Branch Chief
CC:INTL:BR3

SUBJECT: Election under section 962 and the alternative minimum tax

This Chief Counsel Advice responds to your request for advice by e-mail dated November 29, 2001. In accordance with I.R.C. § 6110(k)(3), this Chief Counsel Advice should not be cited as precedent.

LEGEND

Taxpayers =

year one =
year two =
year three =
amount A =
amount B =
amount C =
amount D =
amount E =
amount F =
amount G =
amount H =
amount I =
amount J =
amount K =
amount L =

ISSUES

1. If a taxpayer makes a section 962(a) election for the taxable year, is alternative minimum tax ("AMT") liability with respect to amounts included in income under section 951(a) determined by combining the taxpayer's "regular tax" attributable to that income with the taxpayer's "regular tax" on its other income and comparing the result against the combined tentative minimum tax ("TMT") on such amounts?

2. Is AMT paid pursuant to sections 962(a) and 55 with respect to amounts included in income under section 951(a) allowed as a credit in subsequent years?

3. May Taxpayers revoke their section 962(a) elections if the method of computing the tax due under section 962(a) pursuant to issue one makes the election disadvantageous to them?

CONCLUSIONS

1. No. When a taxpayer makes a section 962(a) election for a taxable year, the determination of whether there is AMT liability with respect to amounts included in income under section 951(a) is made by comparing the taxpayer's "regular tax" attributable to amounts included in income under section 951(a) with its TMT attributable to such amounts.

2. Yes. Subject to applicable limitations, AMT paid pursuant to sections 962(a) and 55 with respect to amounts included in income under section 951(a) is creditable under section 53 in subsequent years.

3. Uncertain. Under Treas. Reg. §1.962-2(c)(2), a section 962(a) election may not be revoked unless a "material and substantial change in circumstances [has] occur[red] which could not have been anticipated when the election was made." We do not have sufficient facts to determine whether Taxpayers would satisfy that regulatory test since they have not applied for approval to revoke their section 962(a) elections for years one, two, and three.

FACTS

Taxpayers are United States shareholders (within the meaning of section 951(b) of the Code) in numerous controlled foreign corporations ("CFCs"). On their joint income tax returns, Forms 1040, for years one, two, and three, Taxpayers timely elected under section 962 and Treas. Reg. §§1.962-1 and 1.962-2 to have income includible in their gross income under section 951(a) taxed at corporate income tax rates under sections 11 and 55 as if those amounts had been received by a corporation rather than at individual income tax rates under sections 1 and 55 ("the election").

Taxpayers attached to their Forms 1040 for years one, two, and three, Forms 1120 and Forms 4626, Alternative Minimum Tax - Corporations. Taxpayers attached the following statement to the Forms 1120:

> This Form 1120 is included as a schedule and is not a stand-alone return. It is included to compute tax under Section 962 for these taxpayers.

The attached Forms 1120 showed combined inclusions of income under section 951(a) with respect to Taxpayers' investments in the CFCs and section 78 gross up amounts to reflect the deemed-paid credits allowed to Taxpayers under the election ("section 962 income"), in the following amounts:

	Year One	Year Two	Year Three
Section 962 income	Amount A	Amount B	Amount C

As a result of making the election, Taxpayers did not include the income that would have otherwise been includible in their income under section 951(a) on their Forms 1040 for years one, two, and three.

The attached Forms 1120 also showed on Schedules J tax due for years one, two, and three which combined the regular corporate income tax plus corporate AMT from Forms 4626. Most of the regular corporate income tax was offset by the allowable foreign tax credits. The following table sets forth the TMT, regular tax (regular corporate income tax reduced by foreign tax credits), and AMT amounts for those years:

Items	Year One	Year Two	Year Three
TMT	Amount D	Amount E	Amount F
Regular Tax	Amount G	Amount H	Amount I
AMT	Amount J	Amount K	Amount L

Taxpayers included on their Forms 1040 for years one, two, and three, as tax due on their section 962 income, only the amount of the regular tax, amounts G, H, and I in the above chart, and not the AMT, amounts J, K, and L in the above chart.

Taxpayers attached a statement to their Forms 1040 which showed that Taxpayers determined the tax due on their section 962 income by comparing the total regular tax on section 962 income from the Forms 1120, Schedules J, Lines 6 (amounts G, H, and I in the above chart) and on non-section 962 income from Forms 1040 with the total TMT on section 962 income from Forms 4626, Lines 13 (amounts D, E, and F in the above chart) and on non-section 962 income from Forms 6251, Lines 26. The statements reflected that this method of comparing the combined tax amounts resulted in a higher regular tax liability for each year. Taxpayers did not pay any AMT for years one, two, and three with respect to either Form 6251, Alternative Minimum Tax- Individuals, or Form 4626.

LAW AND ANALYSIS

1. Determination of the section 962(a) tax

Under section 962 of the Code and Treas. Reg. §§1.962-1 and 1.962-2, an individual United States shareholder of a CFC may elect for a taxable year to be taxed at corporate rates under sections 11 and 55 on amounts included in his or her gross income under section 951(a) and to claim a foreign tax credit for foreign income taxes deemed paid with respect to such amounts under sections 902 and 960. Those deemed paid credits would otherwise have been limited to corporate shareholders.[1]

Section 11 imposes a tax on the taxable income of a corporation. Section 55 imposes an AMT on all taxpayers in addition to a taxpayer's regular income tax liability. Section 55(a) provides that the AMT equals the excess (if any) of the TMT (as defined in section 55(b)) over the regular tax for the taxable year. “Regular tax” means the “regular tax liability for the taxable year (as defined in section 26(b) [and as imposed by section 11]) reduced by the foreign tax credit allowable under section 27(a), the section 936 credit allowable under section 27(b), and the Puerto Rico economic activity credit under section 30A." Section 55(c)(1). Regular tax liability is modified in certain other respects not relevant here.

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[1]Under sections 902 and 960(a)(1), if there is included, under section 951(a), in the gross income of a domestic corporation any amount attributable to the earnings and profits of a foreign corporation at least 10 percent of the voting stock of which is owned by such domestic corporation, such domestic corporation shall be deemed to have paid or accrued the same proportion of the foreign corporation’s post-1986 foreign income taxes which the amount of earnings and profits of such foreign corporation for such taxable year so included in gross income of the domestic corporation bears to such foreign corporation’s post-1986 undistributed earnings.

As discussed above, Taxpayers included as tax due on their section 962 income only the amount of the regular tax, amounts G, H, and I, and not AMT, amounts J, K, and L. Taxpayers determined the tax due by comparing the total regular tax on section 962 income and non-section 962 income with the total TMT on section 962 income and non-section 962 income. The statements which Taxpayers attached to their Forms 1040 for years one, two, and three showed that this method of comparing the amounts of regular tax and TMT resulted in an amount of regular tax that was greater than the amount of TMT for each year. Accordingly, based on their method of computing tax due on section 962 income, Taxpayers did not pay AMT on their section 962 income for those years.

The issue is whether AMT liability with respect to section 962 income should be computed by comparing the regular tax on section 962 income with the TMT on that income or whether it should be computed by comparing the combined regular tax on section 962 income and non-section 962 income with the combined TMT on such amounts. For the reasons discussed below, we have concluded that the AMT liability on section 962 income should be determined by comparing the regular tax with the TMT on the Taxpayers' section 962 income only. Accordingly, the amounts of tax due with respect to Taxpayers' section 962 income are amounts G and J of year one; amounts H and K for year two; and amounts I and L for year three.

When an individual shareholder of a CFC makes a section 962 election for a taxable year, section 962(a) imposes tax at corporate rates on amounts included in income under section 951(a) "as if such amounts were received by a domestic corporation" and allows a credit for foreign taxes deemed-paid with respect to such amounts "as if they were received by a domestic corporation." Consistent with section 962(a)'s treatment of the section 951(a) inclusions being treated as if such amounts were received by a domestic corporation, the amount of tax due on section 962 income should be computed separately from tax due on non-section 962 income. Accordingly, the computation of AMT liability with respect to section 962 income should be done separately.

In addition to being consistent with the express language of section 962(a), this conclusion is also consistent with the statute's purpose. Section 962 was enacted in 1962 as part of the enactment of subpart F of the Code. At that time, the Senate Finance Committee stated that:

> The purpose of this provision [sec. 962] is to avoid what might otherwise be a hardship in taxing a U.S. individual at high bracket rates with respect to earnings in a foreign corporation which he does not receive. This provision gives such individuals assurance that their tax burdens, with respect to these undistributed foreign earnings, will be no heavier than they would have been had they invested in an American corporation doing business abroad. [S. Rept. No. 1881, 1962-3 C.B. at 798.]

Thus, section 962 was enacted to relieve a U.S. individual shareholder of a CFC from a hardship that might otherwise result from a section 951(a) inclusion by ensuring that the tax burden for such individual would be “no heavier” than it would be if the individual had instead invested in a U.S. corporation doing business abroad. If the amount included in income under section 951(a) were derived by a taxpayer’s domestic corporation, such amount would have been subject to tax at the applicable corporate rates. The determination of whether AMT was due with respect to such amount would have been made by comparing the corporation’s regular tax and TMT on that amount. Such determination would not have taken into account the shareholder’s regular tax and TMT on its income.

2. Deduction under section 962(b) and minimum tax credit

Section 962(d) requires a taxpayer, notwithstanding section 959(a)(1), to include in its gross income earnings and profits of a foreign corporation attributable to a section 951(a) inclusion with respect to which a section 962(a) election applied when such earnings and profits are distributed to the extent that the earnings and profits exceed the amount of tax paid under Chapter 1 of Subtitle A of the Code with respect to the section 951(a) inclusion. The determination of the amount that must be included in income under section 962(d) is made separately for distributions from each foreign corporation. See Treas. Reg. §1.962-3. Therefore, a taxpayer cannot reduce the amount that must be included in income when it receives a distribution from one foreign corporation by the amount of tax paid pursuant to section 962(a) with respect to a section 951(a) inclusion attributable to another foreign corporation.

Pursuant to section 962(d), when Taxpayers receive a distribution of earnings and profits attributable to section 951(a) inclusions for years one, two and three, Taxpayers must include those earnings and profits in income. The amount of a distribution by a CFC that must be included in income may be reduced for taxes paid by Taxpayers under sections 11 and 55 as a result of Taxpayer’s section 962(a) elections, but may not be reduced by the taxes paid with respect to section 951(a) inclusions attributable to CFCs other than the CFC making the distribution.

There is an issue as to whether Taxpayers will be allowed to claim a credit for AMT paid for years one, two and three under section 55. In other words, whether Taxpayers will be allowed to claim a credit for amount J paid in year one; amount K paid in year two; and amount L paid in year three.

Section 53(a) allows taxpayers a credit against the tax imposed by Chapter 1 of Subtitle A of the Code for any taxable year in an amount equal to the minimum tax credit (“MTC”) for such taxable year. The MTC for any taxable year is generally the excess (if any) of (1) AMT imposed for all prior taxable years beginning after 1986 (subject to certain adjustments not relevant here), over (2) the amount of MTC allowable for prior taxable years. Section 53(b) and (d). Section 53(c) limits the MTC for any taxable year to the excess (if any) of (1) the regular tax liability for the taxable year reduced by the sum of the credits allowable under subparts A, B, D, E, and F of Subtitle A, Chapter 1A, Part IV of the Code, over (2) the TMT for the taxable year. Accordingly, subject to section 53(c) and other applicable limitations, Taxpayers will be able to claim a MTC for amounts J, K, and L in years subsequent to the year in which they paid those amounts.

3. Revocation of the elections

Section 962(b) provides that a section 962(a) election for the taxable year for which the election is made "may not be revoked except with the consent of the Secretary or his delegate." Treas. Reg. §1.962-2(c)(2) requires taxpayers to apply to the Commissioner for approval to revoke a section 962(a) and provides that approval will not be granted “unless a material and substantial change in circumstances occurs which could not have been anticipated when the election was made.”

Taxpayers have not applied for approval to revoke their elections for years one, two, and three. Therefore, we do not have sufficient facts to determine whether Taxpayers would satisfy Treas. Reg. §1.962-2(c)(2).

Please call (202) 622-3850 if you have any further questions.

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